

## CROMPTON GREAVES

INR 320



Longer term story intact

BUY

Even as operating metrics continues to improve for Crompton Greaves (CRG), revenue growth disappointed for the second quarter in a row. Despite muted revenue growth of 13% Y-o-Y, Q3FY08 PAT of INR 679 mn was however in line with our estimates on account of a strong ~260bps improvement in EBITDA margins. We expect revenues to bounce back in Q4FY08 with the dispatch of a few large jobs, which are likely to result in higher revenue growth. In terms of consolidated results for the quarter, net revenue stood at INR 17.1 bn and PAT at INR 827 mn. For 9MFY08, consolidated net revenues and PAT stood at INR 48 bn and INR 2.6 bn, respectively, translating into EPS of INR 7.1. The cumulative order book was at USD 1.3 bn (INR 52 bn).

\* **Revenues disappoint again; EBITDA margins continue to improve**

For the second quarter consecutively, revenue growth remained subdued at 13% Y-o-Y, to INR 9.2 bn, as few large jobs spilled over to next quarter. The standalone order book was almost flat Y-o-Y, at INR 21.8 bn. However, CRG expects higher order bookings in Q4FY08, which will result in comfortable order book position.

Improving operating performance from all its segments resulted in 42% Y-o-Y growth in EBITDA, to INR 1.2 bn. EBITDA margin improved 260bps Y-o-Y, to 12.7%, due to value engineering of products by using Pauwels' design and own R&D efforts, hedging of commodities, and better utilisation at workshops. PAT, of INR 679 mn (up 50% Y-o-Y), was in line with our expectations.

\* **Downgrading estimates by ~ 8%; earnings expected to grow at 37%**

We are downgrading our FY08E and FY09E consolidated earnings estimates by 8% on account of lower than expected standalone revenue growth, though slightly offset by better EBITDA margins. Incorporating our FY10E estimates, we expect consolidated revenue and earnings to grow at 24% and 37%, respectively, over FY08-10E. The higher earnings growth vis-à-vis revenue growth is on account of expected improvement in operating margins for the standalone entity and subsidiary portfolio. Ganz is expected to turnaround in FY09E and Microsol Holdings is likely to be operational for full year from FY09E.

\* **Outlook and valuations: Long-term story intact; maintain 'BUY'**

On our consolidated EPS of INR 14.8 and INR 19.4, the stock is trading at P/E of 22x and 17x FY09E and FY10E earnings, respectively. We believe the stock price correction, by ~20% from our last quarter result update, more than factors in the disappointment in revenue growth. Given CRG's improving product domain and its move to become a complete solution provider post the MHL acquisition, we are positive on the long-term story of CRG and maintain our 'BUY' recommendation on it.

**Financials (standalone)**

Year to March	Q3FY08	Q3FY07	Change %	Q2FY08	Change %	FY07	FY08E
Revenues (INR mn)	9,152	8,130	12.6	9,050	1.1	33,676	39,459
EBITDA (INR mn)	1,160	818	41.8	1,068	8.6	3,419	4,723
Net profit (INR mn)	679	454	49.5	742	(8.5)	1,924	2,981
Adjusted EPS (INR) *	1.9	1.2	49.5	2.0	(8.5)	5.2	8.1
P/E (x)							39.3
EV/EBITDA (x)							24.7
ROAE (%)							38.1

\* 2:5 bonus in Q3FY07

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Reuters : CROM.BO  
Bloomberg : CRG IN

**Market Data**

52-week range (INR) : 454 / 172  
Share in issue (mn) : 366.6  
M cap (INR bn/USD mn) : 120.7 /2,978.7  
Avg. Daily Vol. BSE/NSE ('000) : 908.9

**Share Holding Pattern (%)**

Promoters : 39.2  
MFs, Fls & Banks : 23.9  
Fls : 16.4  
Others : 20.5

### \* Segmental snapshot

For Q3FY08, all the segments reported modest revenue growth with power systems, contributing ~50% to revenues, reporting only 13% Y-o-Y growth. The lower than expected revenue growth can be attributed to lesser jobs being dispatched in the quarter leading to lower revenue booking. The trend in Y-o-Y margin improvement across segments, which started in Q1FY08, continued in Q3FY08 as well. The industrial systems segment reported EBIT margin of 18.3%, up 405bps Y-o-Y, followed by power systems segment that reported EBIT margin of 12.4%, up 255bps Y-o-Y. The EBIT mix more or less remains unchanged with power systems contributing 46%, industrial systems 37%, and consumer products system 20%.

**Table 1: Segmental break-up of standalone financials**

Year to March	Q3FY08	Q3FY07	Q2FY08	FY07
<b>Y-o-Y growth (%)</b>				
Power systems	13.1	695.1	2.3	714.2
Consumer products	15.0	(50.2)	12.2	(43.8)
Industrial systems	14.0	177.9	14.2	154.9
Others	(34.7)	(76.9)	575.5	(87.1)
<b>Segment revenue mix (%)</b>				
Power systems	47.0	47.0	46.1	48.1
Consumer products	25.9	25.5	25.3	27.0
Industrial systems	26.2	26.0	25.9	24.1
Others	0.9	1.5	2.7	0.8
<b>EBIT margin (%)</b>				
Power systems	12.4	9.9	11.9	10.5
Consumer products	9.8	8.7	10.6	9.6
Industrial systems	18.3	14.3	18.1	14.7
Others	(35.6)	(8.5)	(3.1)	(37.9)
<b>EBIT mix (%)</b>				
Power systems	45.5	44.5	43.1	46.6
Consumer products	19.7	21.3	20.9	23.8
Industrial systems	37.3	35.5	36.7	32.5
Others	(2.5)	(1.2)	(0.7)	(2.8)

Source: Company, Edelweiss research

Financials snapshot (standalone)							(INR mn)	
Year to March	Q3FY08	Q3FY07	change %	Q2FY08	change %	FY07	FY08E	
Revenues (net)	9,152	8,130	12.6	9,050	1.1	33,676	39,459	
Raw material	6,394	5,927	7.9	6,411	(0.3)	24,643	28,239	
Staff cost	455	421	8.1	513	(11.2)	1,743	2,001	
Other operating expenses	1,143	964	18.6	1,058	8.0	3,872	4,497	
Total expenditure	7,992	7,313	9.3	7,982	0.1	30,258	34,736	
EBITDA	1,160	818	41.8	1,068	8.6	3,419	4,723	
Depreciation	115	100	15.2	113	1.7	394	469	
EBIT	1,045	718	45.5	955	9.4	3,025	4,254	
Interest	72	78	(8.0)	60	20.0	304	291	
Other income	144	72	99.7	185	(22.1)	349	623	
PBT	1,117	713	56.8	1,081	3.4	3,070	4,586	
Tax	438	258	69.7	339	29.4	1,146	1,605	
Adjusted net profit	679	454	49.5	742	(8.5)	1,924	2,981	
Reported net profit	679	454	49.5	742	(8.5)	1,924	2,981	
Equity capital(FV:INR2)	733	733	-	733	-	733	733	
# of shares (mn)	367	367	-	367	-	367	367	
Adjusted EPS (INR) *	1.9	1.2	49.5	2.0	(8.5)	5.2	8.1	
<b>as % of net revenues</b>								
Raw material	69.9	72.9	(4.2)	70.8	(1.4)	73.2	71.6	
Staff cost	5.0	5.2	(3.9)	5.7	(12.2)	5.2	5.1	
Other operating expenses	12.5	11.9	5.3	11.7	6.8	11.5	11.4	
EBITDA	12.7	10.1	26.0	11.8	7.4	10.2	12.0	
Adjusted net profit	7.4	5.6	32.8	8.2	(9.5)	5.7	7.6	
Tax rate	39.2	36.3	8.2	31.4	25.1	37.3	35.0	

\* Adjusted for bonus

## Company Description

Mumbai-based CGL, a part of the B M Thapar group, is a pioneer in management and application of electrical energy. It is primarily engaged in designing, manufacturing, and marketing high-technology electrical products and services related to power generation, transmission, distribution, and executing turnkey projects. The company's business comprises three segments viz. power systems, industrial systems, and consumer products. Nearly, two-thirds of its turnover comes from products segment, in which, it enjoys leadership.

## Investment Theme

Given the improving visibility and governments thrust on power sector reforms, we believe that ~68,869 MW of generation capacity is likely to be added in India over the Eleventh Plan, entailing investment of ~INR 4.2 tn. In the backdrop of encouraging investment environment, we remain positive on CGL based on the prospects arising from its second overseas acquisition (Ganz). Post full consolidation of Ganz in FY08, we believe Crompton will not only expand horizontally (geographically), but also vertically (enhanced product portfolio). Amongst the large-cap infrastructure plays in India, Crompton still trades at a relative discount to peers like Siemens, ABB, L&T, and BHEL. We maintain our positive stance on the company.

## Key Risks

Any delay in government spending in the power sector or any major policy change could lead to slowdown in investments from the utility companies, adversely affecting power equipment companies like Crompton.

Higher raw material prices continue to remain a concern for Crompton and could hamper growth in its operating margins, going forward.

Any delay in integration of Ganz and improving operational efficiency of Pauwels' will continue to put pressure on CGL's consolidated performance.

## Financial Statements (Consolidated)

Income statement					(INR mn)
Year to March	FY06	FY07	FY08E	FY09E	FY10E
Income from operations	41,454	56,396	69,044	85,443	105,487
Direct costs	27,764	38,483	45,317	55,637	68,516
Employee costs	5,536	7,171	8,163	10,162	12,653
Other expenses	4,723	5,914	8,978	10,946	13,430
Total operating expenses	38,023	51,569	62,458	76,745	94,599
EBITDA	3,431	4,827	6,586	8,698	10,889
Depreciation and amortisation	762	954	1,272	1,396	1,495
EBIT	2,669	3,873	5,315	7,302	9,393
Interest expenses	360	566	643	614	589
Other income	653	1,053	1,042	1,325	1,677
Profit before tax	2,962	4,360	5,714	8,013	10,481
Provision for tax	493	1,495	1,904	2,581	3,368
Extraordinary items	-	-	-	-	-
Reported profit before minority interest	2,469	2,865	3,810	5,432	7,113
Add: share of profit in associates	41	0	0	0	0
Less: Minority interest	32	47	-	-	-
Reported profit after minority interest	2,478	2,818	3,810	5,432	7,113
Adjusted net profit	2,478	2,818	3,810	5,432	7,113
Shares outstanding	262	367	367	367	367
Dividend per share	1.1	1.5	2.2	3.4	4.5
Dividend payout (%)	12.0	19.3	21.3	22.7	23.1

### Common size metrics- as % of net revenues

Year to March	FY06	FY07	FY08E	FY09E	FY10E
Operating expenses	91.7	91.4	90.5	89.8	89.7
Depreciation	1.8	1.7	1.8	1.6	1.4
Interest expenditure	0.9	1.0	0.9	0.7	0.6
EBITDA margins	8.3	8.6	9.5	10.2	10.3
Net profit margins	6.0	5.0	5.5	6.4	6.7

### Growth metrics (%)

Year to March	FY06	FY07	FY08E	FY09E	FY10E
Revenues	108.3	36.0	22.4	23.8	23.5
EBITDA	104.5	40.7	36.5	32.1	25.2
PBT	129.9	47.2	31.1	40.2	30.8
Net profit	106.0	13.7	35.2	42.6	30.9
EPS	106.0	13.7	35.2	42.6	30.9

### Cash flow statement

Cash flow statement					(INR mn)
Year to March	FY06	FY07E	FY08E	FY09E	FY10E
Net profit	2,469	2,865	3,810	5,432	7,113
Add: Depreciation	762	954	1,272	1,396	1,495
Add: Deferred tax	133	265	138	174	221
Gross cash flow	3,364	4,084	5,220	7,003	8,829
Less: Dividends	418	545	812	1,231	1,643
Less: Changes in W. C.	1,333	1,026	2,083	2,215	2,896
Operating cash flow	1,613	2,513	2,325	3,557	4,290
Less: Change in investments	(85)	(6)	-	-	-
Less: Capex	2,618	6,424	2,513	2,050	1,550
<b>Free cash flow</b>	<b>(921)</b>	<b>(3,905)</b>	<b>(188)</b>	<b>1,507</b>	<b>2,740</b>

<b>Balance sheet</b>		(INR mn)				
<b>As on 31st March</b>	<b>FY06</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>	<b>FY10E</b>	
Equity capital	524	733	733	733	733	
Reserves & surplus	7,330	8,955	11,852	16,054	21,524	
Shareholders funds	7,854	9,689	12,585	16,787	22,257	
Minority interest	117	284	284	284	284	
Secured loans	3,895	8,726	7,134	6,916	6,446	
Unsecured loans	327	319	627	627	627	
<b>Borrowings</b>	<b>4,222</b>	<b>9,045</b>	<b>7,761</b>	<b>7,542</b>	<b>7,072</b>	
<b>Sources of funds</b>	<b>12,192</b>	<b>19,018</b>	<b>20,630</b>	<b>24,614</b>	<b>29,613</b>	
Gross block	17,122	22,332	25,866	27,916	29,466	
Depreciation	11,926	12,480	16,988	18,384	19,879	
Net block	5,196	9,852	8,878	9,532	9,587	
Capital work in progress	207	1,021	0	0	0	
Total fixed assets	5,403	10,873	8,878	9,532	9,587	
Goodwill	-	-	-	-	-	
Investments	651	645	645	645	645	
Inventories	5,959	9,157	8,616	10,252	12,566	
Sundry debtors	10,950	14,213	16,371	20,281	25,389	
Cash and equivalents	2,073	2,417	4,873	6,161	8,431	
Loans and advances	2,206	3,644	3,961	4,891	6,718	
Total current assets	21,188	29,430	33,820	41,584	53,104	
Sundry creditors and others	14,525	20,236	18,862	22,345	27,600	
Provisions	951	2,112	3,337	4,115	5,213	
Total CL & provisions	15,476	22,348	22,200	26,460	32,814	
Net current assets	5,712	7,082	11,621	15,124	20,290	
Net deferred tax	426	418	(513)	(687)	(908)	
<b>Uses of funds</b>	<b>12,192</b>	<b>19,018</b>	<b>20,630</b>	<b>24,614</b>	<b>29,613</b>	
Book value per share (BV) (INR)	30	26	34	46	61	

**Ratios**

<b>Year to March</b>	<b>FY06</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>	<b>FY10E</b>
ROAE (%)	41.2	32.1	34.2	37.0	36.4
ROACE (%)	27.3	24.8	26.8	32.3	34.6
Current ratio	1.4	1.3	1.5	1.6	1.6
Debtors (days)	96	92	87	87	88
Fixed assets t/o (x)	9.3	6.9	7.0	9.3	11.0
Average working capital turnover (x)	9.4	8.8	7.4	6.4	6.0
Average capital turnover (x)	4.2	3.6	3.5	3.8	3.9
Net debt / Equity	0.1	0.3	0.1	0.0	(0.1)
Gross debt/equity	0.5	0.9	0.6	0.4	0.3

**Valuations parameters**

<b>Year to March</b>	<b>FY06</b>	<b>FY07E</b>	<b>FY08E</b>	<b>FY09E</b>	<b>FY10E</b>
EPS (INR)	6.8	7.7	10.4	14.8	19.4
Y-o-Y growth (%)	106.0	13.7	35.2	42.6	30.9
CEPS (INR)	12.4	10.3	13.9	18.6	23.5
P/E (x)	47.2	41.5	30.7	21.5	16.5
Price/BV(x)	10.6	12.1	9.3	7.0	5.3
EV/Sales (x)	3.0	2.2	1.8	1.4	1.2
EV/EBITDA (x)	35.9	25.5	18.7	14.2	11.3

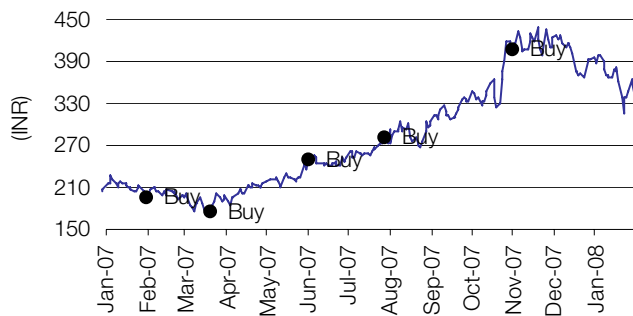
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### Coverage group(s) of stocks by primary analyst(s): Power:

KEI Industries, Apar Industries, Emco, Kalpataru Power Transmission, KEC International, RPG Transmission, Jyoti Structures, ABB, BHEL, Voltas, L & T, Siemens, Suzlon Energy and Crompton Greaves

### Crompton Greaves



Date	Company	Title	Price (INR)	Recos
30-Jan-08	<b>Voltamp Transformers</b>	Leaping ahead; <i>Result Update</i>	1,572	Buy
30-Jan-08	<b>Apar Industries</b>	Temporary setback <i>Result Update</i>	285	Buy
29-Jan-08	<b>Suzlon Energy</b>	Robust order book and positive outlook; <i>Result Update</i>	341	Accum.
28-Jan-08	<b>Techno Elec &amp; Engineering</b>	Clued in the success; <i>Result Update</i>	265	Buy

### Distribution of Ratings / Market Cap

#### Edelweiss Research Coverage Universe

	Buy	Accumulate	Reduce	Sell	Total
Rating Distribution*	110	43	15	2	188

\* 12 stocks under review / 6 rating withheld

	> 50bn	Between 10bn and 50 bn	< 10bn
Market Cap (INR)	88	74	26

### Rating Interpretation

Rating	Expected to
<b>Buy</b>	appreciate more than 20% over a 12-month period
<b>Accumulate</b>	appreciate up to 20% over a 12-month period
<b>Reduce</b>	depreciate up to 10% over a 12-month period
<b>Sell</b>	depreciate more than 10% over a 12-month period

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